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ARTICLE 14 OF CHINA'S NEW LABOR CONTRACT LAW: USING OPEN-TERM CONTRACTS TO APPROPRIATELY BALANCE WORKER PROTECTION AND EMPLOYER FLEXIBILITY

Jovita T. Wang[†]

Abstract: China's economy rapidly developed as it shifted from a planned economy to a market economy. Cheap labor encouraged foreign companies to conduct business in China, but that business came at the expense of labor protection. Workers who had previously enjoyed lifetime employment suddenly faced rampant layoffs, labor abuse, and unemployment. Despite China's implementation of the Labor Law in 1994, labor abuse continued, especially by employers refusing to follow written contract requests to define the employment relationship. Many workers were left unprotected.

In response to these problems, China passed the Labor Contract Law in 2007 to clarify requirements of employment contracts and to inform both employers and workers of their rights and obligations. The law was intended to promote better employment relationships. Article 14 of the Labor Contract Law worked to accomplish this end by allowing the use of open-term employment contracts. Foreign companies and investors, however, have voiced concern that the Labor Contract Law's encouragement of open-term contracts will negatively affect their business in China and make it nearly impossible to dismiss workers. Some of these fears have been realized in South Korea under similar employment laws.

While open-term contracts will inevitably increase some business costs, the benefits of the new Chinese Labor Contract Law outweigh such costs. Because workers will be more invested in business operations, open-term employment contracts will improve employment relationships and make businesses more profitable. Additionally, in contrast to South Korea's employment laws, Article 14 of the Labor Contract Law includes sufficient regulations and flexible requirements to prevent open-term employment contracts from becoming a ticket to lifetime employment. Open-term employment contracts can advance China's economic development.

I. INTRODUCTION

China is experiencing rapid growth while developing into a market economy. Behind the country's economic success, however, lies widespread labor abuse.¹ Workers' main recourse in employment disputes is self-help.² Recruiters often falsely lure migrant workers into abysmal working conditions, where wages are withheld and security guards prevent escape.³

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¹ Sean Cooney, *Making Chinese Labor Law Work: The Prospects for Regulatory Innovation in the People's Republic of China*, 30 *FORDHAM INT'L L.J.* 1050, 1050 (2007).

² *Id.*

³ ANITA CHAN, *CHINA'S WORKERS UNDER ASSAULT: THE EXPLOITATION OF LABOR IN A GLOBALIZING ECONOMY* 7-8 (Mark Selden ed., 2001).

These types of abuses have resulted in domestic and some international pressure on China to reform its labor laws.⁴ The Chinese government has recognized that it must reconcile economic growth with increased “governability, stability, and democracy.”⁵

In 1994, the Standing Committee of the Eighth National People’s Congress (“NPC”) of the People’s Republic of China adopted the Labor Law of the People’s Republic of China (“Labor Law”). China’s passage of the Labor Law was a stride towards creating a harmonious work structure in China’s changing economy.⁶ The Labor Law provided comprehensive rules addressing workers’ rights, labor contracts, discrimination, and social insurance.⁷ Workers, however, still found worker protections inadequate.⁸ The protections of the Labor Law only applied to workers who had a written contract or strong proof of an employment relationship.⁹ Because many employers did not provide such contracts despite being required to do so by the Labor Law, many workers were left unprotected.¹⁰ Often, employers overworked and underpaid their workforce.¹¹ Employers regularly refused to renew contracts.¹² Additionally, the government enforced labor laws inconsistently, especially because provinces and local cities created their own regulations.¹³

On January 1, 2008, China’s new Labor Contract Law (“LCL”) went into effect.¹⁴ The government made improvements to the 1994 Labor Law by changing contractual employment protections and expanding the scope of application.¹⁵ The LCL is the first national law in China governing

⁴ See Cooney, *supra* note 1, at 1050.

⁵ SUJIAN GUO & BAOGANG GUO, *Introduction to CHALLENGES FACING CHINESE POLITICAL DEVELOPMENT* 11 (Sujian Guo & Baogang Guo eds., 2007).

⁶ Labor Law [Labor Law 1994] art. 1 (promulgated by the Standing Comm. Nat’l People’s Cong., July 5, 1994, effective Jan. 1, 1995) LAWINFOCHINA (last visited Nov. 14, 2008) (P.R.C.).

⁷ *Id.*

⁸ See Aaron Halegua, *Getting Paid: Processing the Labor Disputes of China’s Migrant Workers*, 26 BERKELEY J. INT’L L. 254, 274 (2008).

⁹ *Id.*

¹⁰ Haina Lu, *New Developments in China’s Labor Dispute Resolution System: Better Protection for Workers’ Rights?*, 29 COMP. LAB. L. & POL’Y J. 247, 256 (2008).

¹¹ Lyle Morris, *An Uncertain Victory for China’s Workers*, YALE GLOBAL ONLINE, June 24, 2008, <http://yaleglobal.yale.edu/display.article?id=10983> Yale Global (last visited Nov. 14, 2008).

¹² *Draft Law on Labor Contracts Made Public—Views Sought*, XINHUA NEWS AGENCY, Mar. 21, 2006, http://www.china.org.cn/archive/2006-03/21/content_1162551.htm (last visited Feb. 1, 2009).

¹³ Jeffrey A. Blount & Lixin Chen, *Working With China’s New Labor Contract Law*, in *DOING BUSINESS IN CHINA* 129, 131 (Practising Law Institute ed., 2008).

¹⁴ Labor Contract Law [Labor Contract Law] (promulgated by the Standing Comm. Nat’l People’s Cong., June 29, 2007, effective Jan. 1, 2008) LAWINFOCHINA (last visited Nov. 14, 2008) (P.R.C.).

¹⁵ It applies to “all aspects of labor contracts between workers and enterprises, all types of economic entities, and private non-profit entities.” Adam Bobrow et al., *International Legal Developments in Review: 2007*, 42 INT’L LAW. 945, 962 (2008). Xie Liangmin of the All-China Federation of Trade Unions

employment contracts.¹⁶ For instance, it addresses the formation requirements of an employment contract, whereas the previous labor law did not.¹⁷ Under the Labor Law, local tribunals had freedom to implement regulations that reflected their own interpretation of the Labor Law. By contrast, LCL provides guidance to ensure that local regulations will be uniform and consistent with national law.¹⁸ Such uniformity should help companies with operations in more than one city ensure compliance.¹⁹

The LCL aimed to increase worker protection in response to China's fast-paced and capitalist-style economic growth.²⁰ The law passed after the slave labor scandal in the coal mines of Shanxi and Henan provinces.²¹ The government realized that violations of workers' rights, not to mention the resulting strikes, negatively affected social stability and economic development.²² The government passed other employment laws in addition to LCL, such as the Employment Promotion Law.²³ This legislative overhaul demonstrated China's recognition that it must protect workers to

has stated that, "[t]he new law is not designed to replace the current Labor Law; rather, it attempts to further standardize the labor contract in favor of employees." *Labor Law: 'No Giving in to Pressure,'* CHINA DAILY, Jun. 12, 2007, <http://www.china.org.cn/english/China/213567.htm> (last visited Feb. 1, 2009).

¹⁶ *Employees' Rights to be Better Protected*, XINHUA NEWS AGENCY, Dec. 25, 2006, available at http://www.china.org.cn/china/national/2006-12/28/content_1193715.htm.

¹⁷ Sean Cooney et al., *China's New Labour Contract Law: Responding to the Growing Complexity of Labour Relations in the PRC*, 30 UNIV. N.S.W. L. J. 786, 787, 792 (2007).

¹⁸ Joanna Law, *Employment Regulations May Prove a Burden for Employers*, CHINA L. & PRAC., Oct. 2008.

¹⁹ *Id.*

²⁰ See Morris, *supra* note 11.

²¹ *China's Legislature Adopts Labor Contract Law*, XINHUA, Jun. 30, 2007, http://english.people.com.cn/200706/29/eng20070629_388809.html# (last visited Feb. 1, 2009). Migrant workers were forced to work long hours without compensation in illegal mining and brick kilns industries. *Id.* See Joseph Kahn & David Barboza, *China Passes a Sweeping Labor Law*, N.Y. TIMES, Jun. 30, 2007. There was public outcry when the government failed to prosecute many of the responsible officials. Han Dongfang, *The Shanxi Brickyard Scandal and Child Labour in China*, CHINA LAB. BULL., July 25, 2007, <http://www.china-labour.org.hk/en/node/47600> (last visited Feb. 1, 2009).

²² Zana Z. Bugaighis, Comment, *What Impact Will the Revised Trade Union Law of China Have on Foreign Business?*, 16 PAC. RIM L. & POL'Y J. 405, 411 (2007). See also Mortimer B. Zuckerman, *A Giant's Growing Pains*, U.S. NEWS & WORLD REP., Jan. 15, 2006, available at <http://www.usnews.com/usnews/opinion/articles/060123/23edit.htm> (mentioning the higher concentration of economic growth along the coast has resulted in peasant worker strikes in the interior parts of the country).

²³ "The law is enacted to promote employment, promote positive interaction between economic development and increase of employment, and promote the harmony and stability of society." Employment Promotion Law (promulgated by the Standing Comm. Nat'l People's Cong., Aug. 30, 2007, effective Jan. 1, 2008) LAWINFOCHINA (last visited Dec. 18, 2008) (P.R.C.).

prevent future social unrest.²⁴ In many respects, the LCL sought to bring business practices in China more in line with international standards.²⁵

Some foreign companies and investors are concerned that Article 14 of LCL encourages open-term employment contracts. An open-term employment contract is a contract for which the employer and the employee have agreed not to stipulate a definite ending date.²⁶ Two possibilities raise particular concern: first, that the provision will be enforced unfairly against foreign employers; and second, that the provision will increase costs by reducing the ability of businesses to expand and contract when economically necessary. Generally, employers are concerned with LCL's long-term implications for the workforce.

This Comment asserts that while these are valid concerns, particularly in light of the effect of similar labor laws in South Korea, LCL strikes the appropriate and necessary—although imperfect—balance between protecting workers' rights and allowing employers to retain flexibility, which in turn ensures the productivity and profitability of their businesses. The LCL does not create employment for life, nor does it force employers to retain workers when doing so would be detrimental to business. Combined with clarifying regulations, LCL paves a bright path for China's future social and economic development.

Part II of this Comment provides background on the employment changes enacted by the Chinese government and discusses the legislative history behind the 1994 Labor Law and the law's unresolved issues. Part III discusses how the new LCL seeks to resolve the gaps left by the 1994 Labor Law and focuses on Article 14—the provision providing for open-term contracts as well as its implementing regulations. Part IV addresses the possible impact of LCL, particularly Article 14, on foreign businesses, many of which are concerned that the law is too burdensome.²⁷ It also explains the concerns of foreign businesses by analyzing the effects of a similar labor law in South Korea. Part V discusses how LCL alleviates these concerns and contrasts the Chinese Law with the Korean law. Part VI describes the potential benefits of flexible open-term contracts to China's transition from an industrial to a value-added economy.

²⁴ See *A Worker's Manifesto for China; Economics Focus*, THE ECONOMIST, Oct. 13, 2007; St. Council, Notice of the State Council on Doing a Good Job in Promoting Employment (Feb. 3, 2008), available at LAWINFOCHINA (P.R.C.).

²⁵ See Morris, *supra* note 11.

²⁶ Labor Contract Law art. 14.

²⁷ See Morris, *supra* note 11.

II. THE 1994 LABOR LAW INADEQUATELY ADDRESSED THE NEEDS OF CHINA'S WORKERS

China, as a rapidly developing country, has encountered problems with employers abusing the labor force.²⁸ Politicians initially enacted the Labor Law of 1994, which provided a foundation of new worker and employer rights in response to the labor abuses created by the combination of China's economic change to factories and the loss of guaranteed employment.²⁹ The law was made to protect the interests of labor in a way that reflected the societal needs of the developing market economy.³⁰ The Labor Law additionally aspired to establish a uniform body of rules that would equitably govern all employers and workers in China.³¹ Yet the Labor Law of 1994 also left many questions unanswered and was weakly enforced.³²

A. *The Labor Law of 1994 Was Intended to Protect China's Workers in Response to Its Changing Economy*

The Labor Law of 1994 was passed to protect Chinese workers. In the 1950s, the Chinese Communist Party stringently protected employment through its "iron rice bowl" system, which guaranteed lifetime employment.³³ Once China transitioned from a planned economy to a socialist market economy, however, layoffs, unemployment, and labor abuse became rampant.³⁴ In response to these problems, China enacted the Labor Law, which passed on July 5, 1994, and came into effect on January 1, 1995.³⁵ The Labor Law applied to all enterprises and individual economic organizations and protected laborers whose employment was governed by an employment contract.³⁶ Its stated purpose was to implement the Constitutional provisions that protect "the legitimate rights and interests of laborers, readjust labor relationships, establish and safeguard a labor system suited to the socialist market economy, and promote economic development

²⁸ See Bugaighis, *supra* note 22, at 410.

²⁹ K. Lesli Ligorner, 2008: *Year of Broadening Employee Rights and EEO Protections in China*, CHINA L. & PRAC., Jun. 2008.

³⁰ Labor Law 1994 ch. 1.

³¹ See Douglas C. Markel, *Editor's Notes: PRC Labour Law*, CHINA L. & PRAC., Jan. 1994.

³² See *id.*

³³ J. PRYBYLA, *THE CHINESE ECONOMY: PROBLEMS & POLICIES* 132, 173 (2d ed. 1981). See also Bugaighis, *supra* note 22, at 409 (mentioning how jobs were provided by local labor bureaus and included furnished housing and health coverage).

³⁴ Bugaighis, *supra* note 22, at 410.

³⁵ Labor Law 1994.

³⁶ *Id.* art 2.

and social progress.”³⁷ The law was intended to provide worker protections through the usage of employment contracts.

B. The Labor Law of 1994 Failed to Strengthen Worker Protection

Despite the Labor Law’s laudable goals, it did not provide detailed specifications for employment contracts and, thus, failed to increase the ability of contracts to protect workers. For instance, the law did not specify what constitutes an invalid employment contract and did not provide strong regulation of open-term contracts.³⁸ Only Article 20 of the Labor Law discussed the terms of employment contracts and did not specify what constitutes “fixed term, flexible term or taking the completion of a specific amount of work as a term.”³⁹ For example, Article 20 provided that if a laborer works for the “same employing unit for ten years or more and the parties involved agree to extend the term of the labour contract, a labour contract with a flexible term shall be concluded between them if the labourer so requested.”⁴⁰ The law seemed to put the burden on the worker to make the request. Article 20 provided no further information regarding the different requirements for each contract. As a result, the law did not generate clear expectations for employers and workers.⁴¹

In addition, employers failed to follow crucial requirements of the Labor Law, resulting in continued job insecurity. In particular, employers often failed to comply with the Labor Law’s mandatory requirement to create a written contract before establishing a working relationship.⁴² By not providing written contracts, employers avoided supervision by labor bureaus and avoided paying taxes and mandated insurance.⁴³ Employers also retaliated against workers who requested a written contract in accordance with the Labor Law.⁴⁴ Countrywide, as of 2006, it was estimated that seventy percent of rural workers and fifteen percent of urban workers have no contract.⁴⁵ Even workers with contracts often had contracts with terms of

³⁷ *Id.* art. 1.

³⁸ LAW YEARBOOK OF CHINA 2005 489 (Liu Fahe ed., 2005).

³⁹ Labor Law 1994.

⁴⁰ *Id.*

⁴¹ LAW YEARBOOK OF CHINA 2005, *supra* note 38, at 489.

⁴² *See* Halegua, *supra* note 8, at 273-74.

⁴³ *Id.* at 276.

⁴⁴ *See id.*

⁴⁵ Brendan Smith et al., *Multinationals to China: No New Labor Rights (Business Against Labor Rights in China)*, MULTINATIONAL MONITOR (Nov.-Dec. 2006), http://find.galegroup.com/itx/infomark.do?action=interpret&contentSet=IACDocuments&type=retrieve&tabID=T002&prodId=EAIM&docId=A162883794&source=gale&version=1.0&userGroupName=wash_eai&finalAuth=true (last visited Feb. 1, 2009).

three years or less.⁴⁶ For instance, it was estimated that sixty percent of all contracts were for three years or less.⁴⁷ Hence, job security had not improved.

With discontent among workers growing a decade after the Labor Law's passage, the Chinese government began focusing on improving workers' rights.⁴⁸ The government decided to achieve this goal by elaborating on and strengthening the requirements of employment contracts through legislation.

III. THE NEW LABOR CONTRACT LAW OF 2007 ADDRESSES WORKER PROTECTION AND SOCIAL STABILITY IN CHINA'S ERA OF RAPID ECONOMIC DEVELOPMENT

The LCL builds upon the goals of the Labor Law of 1994 by, first, furthering protection of workers' rights and, second, providing a predictable and uniform framework for local tribunals in making employment law decisions.⁴⁹ The first draft of LCL was issued for public comment on March 20, 2006.⁵⁰ After making substantial modifications over the course of four drafts, the Standing Committee of the NPC adopted the final version on June 29, 2007, which became effective January 1, 2008.⁵¹ The LCL applies to all employers doing business in China, regardless of the number of persons employed.⁵² The LCL also seeks to promote "harmonious" relationships between employers and workers and to protect "the lawful rights and interests" of workers.⁵³

A. *The LCL Clarifies the Conditions of Employment Relationships*

In contrast to the Labor Law, LCL clearly stipulates the requirements of an employment relationship through the use of contracts. It provides specific requirements for employment contracts. For instance, LCL requires that all employment contracts be in writing.⁵⁴ It further provides that employers must maintain a written worker handbook stating the basic rules

⁴⁶ *Id.*

⁴⁷ *Id.*

⁴⁸ See *Draft Law on Labor Contracts Made Public—Views Sought*, *supra* note 12.

⁴⁹ See *Putting China's Labour Contract Law into Practice*, CHINA L. & PRAC., Mar. 2008 (translated by Joanna Law).

⁵⁰ Cooney, *supra* note 1, at 1077.

⁵¹ Haina Lu, *supra* note 10, at 248.

⁵² Labor Contract Law art. 2.

⁵³ Labor Contract Law art. 1.

⁵⁴ Labor Contract Law art. 10.

and regulations of employment.⁵⁵ The LCL also states that probationary periods be limited according to the employment contract, with the maximum possible period of six months—a reiteration of the Labor Law of 1994.⁵⁶ The LCL, however, elaborates on time periods when the probation period is reduced.⁵⁷ Additionally, it defines the requirements for mandatory non-competition agreements, making such agreements only applicable to senior management or workers with access to important trade secrets and limiting their duration to two years.⁵⁸

The LCL also provides additional requirements to ensure that employers comply with its requirements for employment contracts. In the hopes of improving employer-worker relations, employers are required to consult with workers or the labor union when deciding on important rules and matters related to the workers, such as working hours, rest days, labor safety, and labor discipline.⁵⁹ Employers may also only terminate workers for cause consistent with the regulations stated in the workers' handbook or in accordance with the law.⁶⁰

The LCL clearly stipulates penalties for violations of the law and provides avenues for workers to protect themselves.⁶¹ This information serves as a deterrent against employers by making the costs of violations clear, predictable, and real. If employers fail to follow the new LCL, they will be subject to administrative fines, awards of double wages, and liability

⁵⁵ See Labor Contract Law.

⁵⁶ Labor Contract Law art. 19; Labor Law 1994 art. 21.

⁵⁷ Labor Contract Law art. 19.

⁵⁸ Labor Contract Law arts. 23-24.

⁵⁹ Labor Contract Law art. 4. "Where an employer formulates, amends or decides rules or important events concerning the remuneration, working time, break, vacation, work safety and sanitation, insurance and welfare, training of employees, labor discipline, or management of production quota, which are directly related to the interests of the employees, such rules or important events shall be discussed at the meeting of employees' representatives or the general meeting of all employees, and the employer shall also put forward proposals and opinions to the employees and negotiate with the labor union or the employees' representatives on an equal basis to reach agreements on these rules or events." *Id.*

⁶⁰ Labor Contract Law art. 39. "Where an employee is under any of the following circumstances, his employer may dissolve the labor contract: 1. It is proved that the employee does not meet the recruitment conditions during the probation period; 2. The employee seriously violates the rules and procedures set up by the employer; 3. The employee causes any severe damage to the employer because he seriously neglects his duties or seeks private benefits; 4. The employee simultaneously enters an employment relationship with other employers and thus seriously affects his completion of the tasks of the employer, or the employee refuses to make the ratification after his employer points out the problem; 5. The labor contract is invalidated due to the circumstance as mentioned in Item (1), paragraph 1, Article 26 of this Law; or 6. The employee is under investigation for criminal liabilities according to law." *Id.*

⁶¹ Labor Contract Law ch. VII. "If the rules and procedure of an employer directly related to the employees' interests is contrary to any laws or regulations, the labor administration department shall order the employer to make ratification and give it a warning. If the rules and procedures cause any damage to the employees, the employer shall bear the liability for compensation." *Id.*

for actual damages.⁶² The law allows workers to sue their employers by giving workers a private right of action, which can be brought in the local employment arbitration bureau or local courts.⁶³ The LCL therefore expands both employers' obligations and workers' rights in comparison to the 1994 Labor Law.

B. The LCL Protects Workers Through Encouragement of Open-Term Contracts, but also Gives Employers Flexibility

Article 14 of LCL protects workers by encouraging, and sometimes even requiring, the increased use of open-term contracts. Open-term contracts continue for an indefinite term until the employer or worker terminates it. Termination of open-term contracts, however, is statutorily governed.⁶⁴ As a result, Article 14 is one of the most hotly contested provisions in LCL because it decreases the ability of employers to terminate at will.⁶⁵

1. The LCL's Article 14 Encourages and Expands Open-Term Contracts

Article 14 of LCL limits the ability of employers to use fixed-term employment contracts, generally requiring that contracts be open-term whenever an employee remains with the same employer for an extended period. Under the 1994 Labor Law, employers could discharge workers either at the expiration of a term contract or for cause.⁶⁶ In the past, employers used short-term contracts to avoid terminating for cause, because an employer could terminate the worker after the stated contractual period without needing to pay severance or provide a reason.⁶⁷ The new LCL limits this practice.⁶⁸ In response, employers are concerned about business flexibility, adaptability, and responsiveness.⁶⁹ Under Article 14, an employer

⁶² Labor Contract Law ch. VII. "If an employer violates this Law by dissolving or terminating the labor contract, it shall pay compensation to the employee at the rate of twice the economic compensations as prescribed in Article 47 of this Law." Labor Contract Law art. 87.

⁶³ Labor Contract Law art. 77. "For any employer whose lawful rights and interests are impaired, he may require the relevant department to deal with the case, apply for an arbitration, or lodge a lawsuit." *Id.*

⁶⁴ Labor Contract Law. See also Jian Hang, *Doing Business in China: Understanding China's Newly Adopted Labor Contract Law*, in *DOING BUSINESS IN CHINA* 107, 109 (Practising Law Institute eds., 2008) (mentioning how there is no employment at-will common law counterpart in China).

⁶⁵ See Morris, *supra* note 11.

⁶⁶ Jian Hang, *Doing Business in China: Understanding China's Newly Adopted Labor Contract Law*, in *DOING BUSINESS IN CHINA* 110 (Practising Law Institute ed., 2008).

⁶⁷ *Id.*

⁶⁸ *Id.*

⁶⁹ *Putting China's Labour Contract Law into Practice*, *supra* note 49.

is permitted to enter, at most, only two fixed-term contracts with a worker.⁷⁰ Severance pay is required for terminating fixed-term contracts, thus adding costs to fixed-term contracts.⁷¹ The restrictions on fixed-term contracts encourage more employers to use open-term contracts with workers, which provide more protections.⁷²

In comparison to the Labor Law, LCL's Article 14 defines more clearly those situations when open-term contracts are created. The Labor Law mentioned open-term contract requirements only in passing, under Article 20. Article 20 of the Labor Law required mandatory open-term contracts when a worker had worked for the same employer for ten or more years and that worker formally requested an open-term contract from the employer.⁷³ Now, LCL provides detailed information to help employers navigate open-term contracts. The relevant provision of LCL's Article 14 states: "The labor contract with unfixed terms shall be concluded unless laborers request the conclusion of a labor contract with fixed terms . . . [w]here a labor contract with fixed terms has been concluded for two consecutive times."⁷⁴ After the expiration of a second-term contract, the subsequent employment contract is considered an "open-term contract," under which the worker will be employed until he or she decides to terminate the contract, reaches retirement age, or until certain circumstances occur that give rise to termination.⁷⁵ Under Article 14, an open-term contract also results when the worker has been working for the employing unit for ten consecutive years, and in circumstances when contracts have been re-concluded due to a restructuring but the worker has been working for the employing unit ten consecutive years and is less than ten years from the statutory retirement age.⁷⁶ These examples illustrate LCL's expanded use of open-term contracts.

2. *The LCL Considers Employers' Interests by Providing Safeguards to Prevent "Employment for Life"*

Aware that mandating open-term contracts could harm business, the National People's Congress, the country's legislative body, attempted to balance both the goals of employers and workers in the drafting of LCL.

⁷⁰ Labor Contract Law art. 14.

⁷¹ Labor Contract Law art. 46.

⁷² Jian Hang, *supra* note 66, at 110.

⁷³ Labor Law 1994 art. 20.

⁷⁴ Labor Contract Law art. 14.

⁷⁵ *See generally* Labor Contract Law art. 14.

⁷⁶ Labor Contract Law art. 14.

The first draft of LCL stated that a labor relationship without a written contract would be “regarded as a long term labor relationship unless the worker expresses otherwise.”⁷⁷ Article 14 seems to enact a compromise between the two parties, by providing that, after one year, a labor relationship without a written contract would be considered an employment contract of indefinite term.⁷⁸ Hence, an employer does have some flexibility in creating employment contracts and not all default contracts will be open-term.

In response to business concerns that Article 14 reverts back to the “iron rice bowl system” of imposing lifelong employment, China’s State Council, the country’s Cabinet equivalent, issued an implementing regulation for LCL.⁷⁹ The Implementing Regulation of LCL provides more guidance in interpreting LCL, including Article 14.⁸⁰ The Council’s goal in drafting the regulations was to assure employers that an open-term employment contract would not be an “iron rice bowl”, and that employers could still dismiss workers if they had proper grounds.⁸¹

The Council’s regulations for LCL provide flexible circumstances for worker termination.⁸² The regulations took immediate effect on September 18, 2008.⁸³ With respect to Article 14 of LCL, the regulations explicitly provide the exceptions under which an employer can terminate a worker with an open-term contract.⁸⁴ The regulations clarify the applicability of fourteen circumstances listed in Article 19 of the regulations, stating that an employer may terminate an open-ended contract under any of the listed circumstances.⁸⁵ Thus, the regulations make clear that LCL’s list of fourteen permitted termination circumstances applies to open-term contracts.⁸⁶

Most importantly, the regulations provide employers and workers the ability to negotiate termination of an open-term contract. The first allowed

⁷⁷ Haina Lu, *supra* note 10, at 257.

⁷⁸ Labor Contract Law art. 14.

⁷⁹ *New Regulation Clears Labor Contract Law Misunderstanding*, XINHUA NEWS AGENCY, Sept. 19, 2008, http://www.china.org.cn/business/news/2008-09/19/content_16503117.htm (last visited Nov. 15, 2008).

⁸⁰ *Id.*

⁸¹ *Id.*

⁸² *Id.*

⁸³ *Contract Law 'Boost for Social Security,'* CHINA DAILY, Sept. 20, 2008, available at http://www.china.org.cn/government/news/2008-09/20/content_16508773.htm.

⁸⁴ *Labor Contract Law 'Unfairly Criticized,'* CHINA DAILY, Mar. 12, 2008, available at http://www.china.org.cn/government/NPC_CPPCC_sessions2008/2008-03/12/content_12338793.htm.

⁸⁵ Regulation on the Implementation of the Employment Contract Law [Regulations] art. 19 (promulgated by the State Council, Sept. 3, 2008, effective Sept. 18, 2008) LAWINFOCHINA (last visited Nov. 14, 2008) (P.R.C.).

⁸⁶ See Regulations art. 19; Labor Contract Law arts. 39-41.

circumstance for termination is based on a negotiated consensus between the employer and the worker.⁸⁷ It allows for termination if both parties agree to termination. It is possible that under this exception, employers might force workers to agree to terminate the open-term contract. At the very least, however, the regulations here give employers and workers the ability to bargain about the termination of an open-term contract. Unlike the “iron rice bowl” system, both parties are not required to stay together if they wish otherwise.

The regulations also empower employers to terminate open-term contracts due to worker actions during the employment period. The second enumerated circumstance allows termination when “the employee is proved to have failed to meet the employment conditions during the probation.”⁸⁸ The third and fourth circumstances allow for termination when the “employee seriously violates the rules and procedures set up by the employer” or “the employee seriously neglects his duties or engages in malpractice for personal gains and has caused severe damages to the employer.”⁸⁹ The fifth listed circumstance permits termination when “the employee simultaneously enters an employment relationship with any other employer and thus seriously affects his completion of the tasks assigned by the employer, or the employee refuses to correct after the employer has pointed out the problem.”⁹⁰ Pursuant to the above circumstances, employers can terminate unsatisfactory workers.

Circumstances six and seven permit termination based on criminal or otherwise illegal actions of the worker—even when the actions in question did not occur during work. The sixth circumstance allows termination if the employment contract was procured illegally.⁹¹ Integrating item one in LCL’s Article 26, the regulation states that an employment contract is invalid if “the employee, by means of deception or coercion or by taking advantage of the employer’s difficulties, forces the employer to conclude or change the employment contract against the employer’s true will.”⁹² Under LCL, if a dispute over the validity of a contract arises, either the labor dispute arbitration authority or the people’s court makes the determination.⁹³ The seventh circumstance allows for termination when “the employee is under

⁸⁷ Regulations art. 19.

⁸⁸ *Id.*

⁸⁹ *Id.*

⁹⁰ *Id.*

⁹¹ *Id.*

⁹² *Id.*

⁹³ Labor Contract Law art. 26(3).

investigation for criminal liabilities.”⁹⁴ Employers are not required to retain a worker when the worker’s actions have shown a potential harm to the business.

The Council regulations also empower employers to terminate employees based on circumstances that may be beyond the worker’s control. Circumstances eight and nine consider situations when it is no longer feasible for the worker to continue the employment relationship.⁹⁵ For instance, the relationship can be terminated when “the employee is sick or is injured for a non-work related reason and cannot resume his original position after the expiration of the prescribed time period for medical treatment, nor can he assume any other position arranged by the employer.”⁹⁶ A worker can also be terminated when he or she “is incompetent for his position and is still so after training or being assigned to another position.”⁹⁷ These circumstances provide that while an employer is initially required to accommodate the worker, if such accommodations do not work, the employer may have grounds for termination. Although employers would need to provide some severance payment, they are not obligated to retain incapable workers.⁹⁸

External changed circumstances can also provide the basis for termination. Circumstance ten states that if there is a major change in the objective circumstances relied upon at the time the employment contract was executed, the contract might be voidable.⁹⁹ Circumstance ten only applies if the contract terms cannot be performed and both the worker and employer are unable to reach an agreement on amending the existing employment contract.¹⁰⁰ An employer can also terminate the contract if it experiences “serious difficulties in production and business operations.”¹⁰¹ If the employer changes its production activity in an enterprise—e.g. introducing a material technology innovation or adjusting its operation—it may be allowed to fire workers.¹⁰² Such termination, however, depends on whether the employer has amended employment contracts and, nevertheless, finds reduction in its workforce necessary.¹⁰³ Additionally, the regulation includes a catchall, stating that termination may be granted when there are “other

⁹⁴ Regulations art. 19.

⁹⁵ *Id.*

⁹⁶ Regulations art. 19(8).

⁹⁷ Regulations art. 19(9).

⁹⁸ *See* Labor Contract Law.

⁹⁹ Regulations art. 19.

¹⁰⁰ *Id.*

¹⁰¹ Regulations art. 19(12).

¹⁰² Regulations art. 19(13).

¹⁰³ *Id.*

objective economic situations in which the employment contract is based change substantially, which makes it impossible to perform the employment contract.”¹⁰⁴ The regulation also allows termination when the “employer is being restructured according to the Enterprise Bankruptcy Law.”¹⁰⁵

The regulations implementing LCL address multiple situations in which an employer can terminate a worker with an open-term contract. The regulations enumerate possible economic situations where an employment relationship may be terminated because it no longer benefits the business. The regulations do not force employers to retain workers should the business change its employment needs, nor do they require employers to retain workers who commit crimes or who become unable to perform required job duties.

3. *The LCL Regulations Guide the Implementation Timeline for Open-Term Contracts, Protecting Workers and Providing Notice to Employers*

In an effort to clarify potential misunderstandings between employers and workers, the regulations provide additional guidance as to when a contract becomes open-ended. As noted above, Article 14 of LCL provides that an open-term contract is created once a worker remains with an employing unit for ten consecutive years. The regulations spell out how this ten-year requirement is calculated. The Labor Law had no such guidance. Article 9 of LCL regulations stipulates that the time period begins on the date the employer started using the worker, even if that date occurred prior to the new LCL.¹⁰⁶ As mentioned earlier, the conditions requiring open-term contracts under Article 14 exist when a second fixed-term contract expires, or when the worker has been working for the same employer for ten consecutive years.¹⁰⁷ While LCL’s Article 14 strongly supports open-term contracts, a fixed-term contract seems to be the default rule for renewals unless the stipulations under Article 14 apply. Hence, employers are not stuck with open-term contracts when they first hire a worker so long as they create a contract within a year.¹⁰⁸

¹⁰⁴ Regulations art. 19(14).

¹⁰⁵ Regulations art. 19(11). *See also* Enterprise Bankruptcy Law (promulgated by the Standing Comm. Nat’l People’s Cong., Aug. 27, 2006, effective Jun. 1, 2007) LAWINFOCHINA (last visited Dec. 21, 2008) (P.R.C.).

¹⁰⁶ Regulations art. 9.

¹⁰⁷ Labor Contract Law art. 14.

¹⁰⁸ *See* Labor Contract Law art. 14.

The LCL regulations further state that while an open-term employment contract has no definite ending date, the contract is not preserved if valid reasons exist for its termination.¹⁰⁹ In practice, then, open-term contracts have significant similarities to regular contracts. Open-term contracts provide sufficient flexibility for employers to adjust their workforce. Additionally, the regulations provide a framework for local and provincial tribunals to implement their own regulations consistent with LCL. They do not amount to a reversion to China's "iron rice bowl" system.

However, despite these efforts to clarify Article 14, some foreign companies are wary of the law's implications.

IV. FOREIGN CORPORATIONS ARE CONCERNED ABOUT INCREASED COSTS THAT MAY RESULT FROM OPEN-TERM CONTRACTS, INCLUDING DISCRIMINATORY ENFORCEMENT OF LCL

Foreign corporations in China have expressed concern that LCL will be enforced disproportionately against them, increasing business costs and making investment in China less desirable.¹¹⁰ They are particularly concerned about Article 14's imposition of open-term contracts.¹¹¹ While it is true that most of these concerns arose before passage of LCL's regulations, some of these concerns remain valid—especially in light of experiences in Korea, which has labor laws similar to China's.

A. *Foreign Employers Are Concerned that LCL Unfairly Targets Them*

Based on past experience, foreign employers fear that enforcement actions will disproportionately target them. Reports indicate that foreign companies generally comply with Chinese laws and that most worker abuse occurs at Chinese-owned firms.¹¹² In fact, one of the critiques of the Labor Law of 1994 was that its lax and unfair enforcement put complying companies at a competitive disadvantage.¹¹³ Foreign companies newly operating in China cite unclear regulations as one of the biggest challenges

¹⁰⁹ Sino-Link Consulting, Implementation Regulation for Law of the People's Republic of China on Employment Contracts Effective, <http://www.hg.org/article.asp?id=5453> (last visited Nov. 15, 2008).

¹¹⁰ Aaron Halegua, *The Debate Over Raising Chinese Labor Standards Goes International*, 1 HARV. L. POL'Y. REV. (Apr. 5, 2007), http://www.hlpronline.com/2007/04/halegua_01.html (last visited Jan. 30, 2009) [hereinafter Halegua, *The Debate*].

¹¹¹ *Id.*

¹¹² US-China Business Council Staff, *The New Labor Contract Law*, 34 CHINA BUS. REV. 42, 43 (2007).

¹¹³ David Barboza, *China Drafts Law to Boost Unions and End Labor Abuse*, N.Y. TIMES, Oct. 13, 2006, at A1.

to conducting business.¹¹⁴ Some critics believe that the main issue is not that Chinese laws lack worker protection but, rather, that enforcement of such laws is poor.¹¹⁵ Such inconsistency in enforcement and implementation generally discourages businesses from investing and expanding operations.¹¹⁶

B. Foreign Employers Are Concerned that LCL Will Make it More Difficult to Terminate Workers, Resulting in Additional Costs

Foreign employers are also concerned that LCL's new requirements, especially those governing termination, will significantly increase costs and decrease China's competitive value. The law does make termination more difficult, potentially raising costs. Some companies, seeking less regulation, have moved operations from China to other countries.¹¹⁷

1. As a Result of the LCL, Some Foreign Employers Have Either Left or Have Contemplated Leaving China

The LCL has adversely affected small and medium size companies, especially in labor-intensive industries that adapt to change slowly.¹¹⁸ Since the law's enactment, some companies have left the country or found new places to outsource their operations. For instance, some foreign companies have left China to set up operations in countries with fewer worker protections—such as Vietnam, Bangladesh, and Cambodia—to cut costs; this trend is found most in those businesses with many labor-intensive tasks.¹¹⁹ The LCL especially impacts smaller, labor-intensive Taiwanese and Hong-Kong owned manufacturers because they have relied on China's cheap labor supply.¹²⁰ Surveys from the American Chamber of Commerce and the consulting firm Booz Allen Hamilton indicate that foreign investors plan to move some of their operations out of China as a result of the law's passage.¹²¹

¹¹⁴ AmCham-China, *Part One The Business Climate for American Firms in China*, 2008 WHITE PAPER 12, 14.

¹¹⁵ Halegua, *The Debate*, *supra* note 110.

¹¹⁶ AmCham-China, *supra* note 114, at 26.

¹¹⁷ Halegua, *The Debate*, *supra* note 110.

¹¹⁸ *Putting China's Labour Contract Law into Practice*, *supra* note 49.

¹¹⁹ *See* Morris, *supra* note 11. For instance, Nike has been shifting some production facilities to Vietnam. *Id.*

¹²⁰ Jonathan Adams & Ko Shu-ling, *China: Judgment Day*, 171.2 FAR E. ECON. REV. 32 (2008).

¹²¹ Megan Shank, *Dealing With It: MNCs Learn to Cope with the Labor Law*, MEGAN SHANK DOT COM, Jun. 1, 2008, <http://www.meganshank.com/articles/dealing-with-it/> (last visited Feb. 25, 2009). Booz Allen Hamilton, a management consulting firm, and the American Chamber of Commerce Shanghai, a

Open-term contracts stand as a major reason for corporate flight, as evidenced by the fact that foreign companies both took steps to avoid open-term contracts before LCL's passage and opposed the open-term provisions of LCL. Foreign companies took special umbrage at LCL's required severance payments in certain worker terminations.¹²² For instance, prior to the enactment, a few companies asked their workers to resign and then sign a new two-year contract to avoid Article's 14 impositions of indefinite contracts, for example the French company, Carrefour.¹²³ Even a domestic corporation, Huawei Technologies Co., attempted to terminate employment contracts with more than 7,000 workers before the law's effective date in an effort to dodge signing open-ended employment contracts.¹²⁴ After talks with the All China Federation of Trade Unions, Huawei later suspended its plan.¹²⁵ These examples demonstrate that at least some employers are hesitant about the impact of open-term contracts. Employers detest paying severance packages and fear costly litigation over whether a worker was rightfully terminated.¹²⁶

Yet, other variables besides the implementation of LCL explain the hardships facing labor-intensive businesses. The rising value of the Yuan, an increase in Chinese business taxes, and more protective environmental regulations have also encouraged companies to locate operations elsewhere.¹²⁷ In addition, prior to the global economic downturn of 2008, higher material costs were exerting pressure on the profits of many industries.¹²⁸ Because of these confounding factors, the impact of LCL's passage is hard to isolate. Even so, it seems likely that LCL explains some corporate flight from China.

leading international business association in China, surveyed 66 of the largest foreign-owned and invested manufacturers in China from September-November 2007. See *Booz Allen/AMCHAM Shanghai Study Finds Companies Adopting China as Both a Growth Market and Manufacturing Hub Are Two-Thirds More Profitable Than Others*, BOOZ ALLEN HAMILTON, Mar. 4, 2008, http://www.boozallen.com/news/china_manufacturing_2008 (last visited Feb. 25, 2009).

¹²² Labor Contract Law.

¹²³ See Morris, *supra* note 11.

¹²⁴ Chen Hong, *Maneuver on Labor Law Faces Block*, CHINA DAILY, July 22, 2008, available at <http://english.people.com.cn/90001/6455167.html>.

¹²⁵ *New Regulation Clears Labor Contract Law Misunderstanding*, XINHUA NEWS AGENCY, Sept. 19, 2008, available at http://www.china.org.cn/business/news/2008-09/19/content_16503117.htm.

¹²⁶ See Morris, *supra* note 11. See also Blount & Chen, *supra* note 13, at 136 (discussing employers who had previously implemented rules that avoided overtime payments are concerned about the severance payments imposed by LCL).

¹²⁷ Adams & Ko Shu-ling, *supra* note 120.

¹²⁸ *Id.*

C. *Employers Are Concerned About Similarities Between South Korea's Strict Labor Laws and China's LCL*

China's LCL has similarities to South Korea's main governing employment law, the Labor Standards Act ("LSA").¹²⁹ For instance, the LSA limits term contracts and requires a difficult standard of "just cause" for termination of open-term employment contracts.¹³⁰ The LSA has been unequally enforced against foreigners and has proven inflexible for foreign employers.¹³¹ South Korea has a reputation of having stringent and inflexible employment laws.¹³² It even has higher employment protection compared with other countries under the Organisation for Economic Co-Operation and Development.¹³³ Similarities between LSA and LCL seem to validate concerns that LCL will result in problems like those faced in South Korea—especially given the similar history of labor relations in the two countries.¹³⁴

1. *South Korea's Employment Law Limits Employers' Ability to Terminate Workers*

In South Korea, employers do not have much flexibility to terminate workers with open-term contracts and need "just cause."¹³⁵ South Korea's LSA sets a high standard for grounds of a termination to qualify as "just cause."¹³⁶ Due to this high standard of protection, employers generally use temporary and fixed-term contract workers. This leads to increased inequity, as more temporary and fixed-term workers are employed without the same

¹²⁹ Labor Standards Act, No. 5309 (Mar. 13, 1997) (S. KOR.).

¹³⁰ Jeong Han Lee, *South Korea: Key Limits on Employer Latitude in Structuring Workforce*, MONDAQ, Mar. 20, 2007, <http://www.mondaq.com/article.asp?articleid=46866> (last visited Feb. 6, 2009).

¹³¹ Kim Wan-soon & Lee You-il, *South Korea: The Chill Wind of Korean Xenophobia*, 168.11 FAR E. ECON. REV. 41 (2005).

¹³² Jeong Han Lee, *supra* note 130.

¹³³ John P. Martin & Raymond Torres, *Korean Labor Market and Social Safety-Net Reforms: Challenges and Policy Requirements*, in LABOR MARKET REFORMS IN KOREA: POLICY OPTIONS FOR THE FUTURE 358, 378 (Funkoo Park et al. eds., 2001).

¹³⁴ Korea also faced the same problems as China with the shift from lifetime employment to market-driven employment. Brett M. Kitt, *Downsizing Korea? The Difficult Demise of Lifetime Employment and the Prospects for Further Reform*, 34 LAW & POL'Y INT'L BUS. 537, 540-543 (2003). Much of Korea's significant economic development in 1980's was due to its cheap labor supply and repressed labor rights. Young-bum Park, *Editorial Introduction*, in LABOR IN KOREA (Korea Labor Institute, eds., 1993).

¹³⁵ Labor Standards Act, No. 5039, art. 23 (Mar. 14, 1997) (S. KOR.).

¹³⁶ Chun-Wook Hyun & Scott Balfour, *Labor Standards Act—Defining Rights and Responsibilities*, in KOREAN LABOR AND EMPLOYMENT LAWS: AN ONGOING EVOLUTION 31, 37 (Korea Labor Institute eds., 1998).

benefits and job security as employees with open-term contracts.¹³⁷ Similarly, China's LCL provides strong protections for workers with open-term contracts, which could result in Chinese employers opting to hire workers for the short-term rather than for the long-term.

The use of fixed-term contracts in South Korea has created inequitable results, which has led to disruptive protests, demonstrations, and strikes by workers.¹³⁸ These events have also reduced business profitability.¹³⁹ Employers have justified hiring temporary and fixed-term contract workers with the lower cost of such workers, which is estimated to be forty-four percent lower than regular workers.¹⁴⁰ However, the productivity of temporary and fixed-term contract workers is estimated to be twenty-two percent below regular workers with indefinite contracts.¹⁴¹ These hiring practices have contributed to worker disgruntlement. A 2005 government survey showed that while eighty percent of regular workers were satisfied, only twenty-nine percent of non-regular workers were satisfied.¹⁴² Surveys also showed limited mobility between regular and non-regular employment. In 2003, only fifteen percent of non-regular workers transitioned to regular employment.¹⁴³ High turnover rates result, with sixty-two percent of non-regular workers having less than one year of tenure; in comparison, only thirty percent of regular workers last less than one year.¹⁴⁴ Employers also provided less training to non-regular workers, probably because employers are not required to provide such services to non-regular workers.¹⁴⁵ Non-regular workers also lack protection from unions.¹⁴⁶

All of these factors contributed to a volatile South Korean workforce dissatisfied with LSA's effects. The stringent regulations ultimately harmed both employees and employers.¹⁴⁷ Big corporations like Hyundai lost a few days of productivity from worker strikes.¹⁴⁸ In response, South Korea

¹³⁷ RANDALL S. JONES, ORG. FOR ECON. CO-OPERATION AND DEV., PUBLIC SOCIAL SPENDING IN KOREA IN THE CONTEXT OF RAPID POPULATION AGEING 41 (2008).

¹³⁸ Kitt, *supra* note 134, at 547, 556.

¹³⁹ *Id.*

¹⁴⁰ JONES, *supra* note 137, at 41.

¹⁴¹ *Id.*

¹⁴² *Id.* at 43.

¹⁴³ *Id.*

¹⁴⁴ *Id.*

¹⁴⁵ *Id.* See also Kitt, *supra* note 134, at 560-61 (mentioning how employers are not obligated to provide benefits such as job training for temporary employees, thereby avoiding the protective provisions under LSA).

¹⁴⁶ Kitt, *supra* note 134, at 560-61.

¹⁴⁷ *Id.* at 557.

¹⁴⁸ *Id.* at 556. See also C. Jay Ou, *Democracy on Trial: South Korean Workers Resist Labor Law Reform*, *Multinational Monitor*, 18.3 MULTINAT'L MONITOR 14, 14-15 (1997) (where close to 400,000

passed the Act on Protection of Temporary and Part-time Workers in July 2007.¹⁴⁹ Under that act, a temporary worker with a limited-term contract, who works for more than two years, is automatically regarded as having an open-term contract after the term contract ends.¹⁵⁰ The experience of South Korea fuels concerns that employers in China will also try to bypass the increased protections of LCL—a condition that would only exacerbate China’s worker inequality problem.

2. *Critics Contend that South Korea’s Employment Laws Are Unfairly Enforced Against Foreign Corporations Due to Inadequate Implementation Guidelines—A Concern also Raised by China’s LCL*

Legal analysts have criticized South Korea’s employment laws for not providing clear guidelines. Often, this ambiguity has caused employers to hesitate in termination decisions for fear of litigation.¹⁵¹ For instance, the LSA does not explicitly define “just cause” for the termination of open-term contracts. Some possible examples from case law include “lack of aptitude, continuing defective work, debilitating disease, breach of employment contract, egregiously unacceptable behavior on the job, misrepresentation of previous school or work experience, or an improper relationship with another worker,” but the law itself does not provide any specifics.¹⁵² In 1997, at the request of the International Monetary Fund, a managerial urgency requirement was inserted into LSA, allowing termination of a worker for administrative reasons.¹⁵³ Yet the managerial urgency requirement clause remains ambiguous. It states that the requirement is permitted when there is an “urgent administrative necessity for the transfer, merger, or acquisition of the business in order to prevent administrative deterioration.”¹⁵⁴ The clause fails to clarify whether transfers, acquisitions, and mergers are illustrative or exhaustive of the types of business conditions that permit dismissal.¹⁵⁵

Because of its unclear guidelines and lack of flexibility, critics claim that LSA unfairly impacts foreign corporations doing business in South Korea. Foreign investors have cited South Korea’s “inflexible labor laws”

unionists in the heavy industry sectors held nationwide strikes that caused hundreds of factories to temporarily suspend production).

¹⁴⁹ Act on the Protection of Fixed-term and Part-time Employees, No. 8074 (2006) (S. KOR.).

¹⁵⁰ Jeong Han Lee, *supra* note 130.

¹⁵¹ Kitt, *supra* note 134, at 553.

¹⁵² Chun-Wook Hyun & Scott Balfour, *supra* note 136, at 38.

¹⁵³ Kitt, *supra* note 134, at 549-550.

¹⁵⁴ Labor Standards Act, No. 5039, art. 31 (Mar. 14, 1997) (S. KOR.).

¹⁵⁵ Kitt, *supra* note 134, at 553-554.

and “volatile labor-management relations” as significant impediments to investment.¹⁵⁶ South Korea’s reputation for having a “violence-prone labor force” is another major reason why foreigners are discouraged to directly invest.¹⁵⁷ Additionally, the Korean labor market is generally the most consistent worry for foreign multinational corporations, because they believe it disadvantages management.¹⁵⁸ The situation in South Korea might therefore fuel concerns that open-term contracts and strict termination guidelines will also prove harmful to foreign business in China.

For instance, in certain areas China’s LCL regulations are vague and could be abused. The LCL regulations require that in open-term employment contracts both laborer and employer shall observe the principle of equality and reasonability to decide the content of the labor contract other than the term.¹⁵⁹ Like the Korean law, the regulations do not provide a definition or guide to determine what qualifies as a principle of “equality and reasonability.” In addition, it is unclear what exactly counts as “serious” or “material” under the fourteen permitted circumstances listed under LCL’s implementing regulations.¹⁶⁰ The regulations do provide some examples of what types of conduct is “serious” and “material” sufficient to justify dismissal of open-term employees (such as providing information to an employer’s competitor), based on Article 19 of LCL’s implementing regulations but fail to give guidance to courts as to how they should reach a determination in a particular instance. In some ways, the regulations merely repeat provisions already stated in LCL without more elaboration. Hence, labor tribunals may have to issue their own regulations of interpretation, which could make implementation of LCL less uniform.¹⁶¹

Additionally, while the regulations allow termination based on objective, changed circumstances, the regulations do not explicitly refer to Article 41 of LCL, which describes some such circumstances. This failure to refer creates significant dissonance. Article 41 of LCL requires that when an employer terminates workers based on a restructuring (in accordance with the Enterprise Bankruptcy Law), a serious difficulty in production and operation, or a change that causes the nonperformance of an employment

¹⁵⁶ BuyUSA.gov, Investment Climate Statement, http://www.buyusa.gov/korea/en/investmentclimate.html#_section12 (last visited Feb. 6, 2009).

¹⁵⁷ Kitt, *supra* note 134, at 563.

¹⁵⁸ Kim Wan-soon & Lee You-il, *supra* note 131.

¹⁵⁹ Regulations art. 11. “The contents of an employment contract shall be determined by both parties under the principles of legality, equity, free will, consensus, and good faith.” *Id.* Similar guidelines are also repeated in Article 3 of LCL.

¹⁶⁰ See Part III.B.2.

¹⁶¹ Law, *supra* note 18.

contract, the employer must terminate workers on a priority basis.¹⁶² The last workers to be terminated would be those who have executed an employment contract with a relatively long fixed-term or an open-term employment contract, or those who are the sole breadwinner of their family and must support elders or minors. Moreover, if the employer must terminate twenty or more workers, or more than ten percent of the total workers, the employer is required to report to the labor union or all workers thirty days in advance.¹⁶³ Because the regulations, when listing the circumstances related to objective, changed circumstances, fail to refer to the remaining requirements of Article 41 of LCL, it is unclear whether these requirements apply.¹⁶⁴

The regulations are also unclear on whether an employer has the right not to renew a second fixed-term contract.¹⁶⁵ If employers do not have the right to refuse renewing a second fixed-term contract, then employers will likely be more reluctant to offer a second fixed-term contract, because to do so would essentially create an open-term contract for the worker. If such is the case, employers are only provided one fixed-term contract where they are not obligated to give out an open-term contract. In addition, while the regulations provide guidance on how to calculate time for the ten-year period, they do not address nuances such as when a company merges with another.¹⁶⁶

¹⁶² Labor Contract Law art. 41. "Under any of the following circumstances, if it is necessary to lay off 20 or more employees, or if it is necessary to lay off less than 20 employees but the layoff accounts for 10% of the total number of the employees, the employer shall, 30 days in advance, make an explanation to the labor union or to all its employees. After it has solicited the opinions from the labor union or of the employees, it may lay off the number of employees upon reporting the employee reduction plan to the labor administrative department: 1. It is under revitalization according to the Enterprise Bankruptcy Law; 2. It encounters serious difficulties in production and business operation; 3. The enterprise changes products, makes important technological renovation, or adjusts the methods of its business operation, and it is still necessary to lay off the number of employees after changing the labor contract; or 4. The objective economic situation, on which the labor contract is based, has changed considerably and the employer is unable to perform the labor contract. The following employees shall be given a priority to be kept when the employer cuts down the number of employees: 1. Those who have concluded a fixed-term labor contract with a long time period. 2. Those who have concluded a labor contract without fixed term; and 3. Those whose family has no other employee and has the aged or minors to support. If the employer intends to hire new employees within 6 months after it cuts down the number of employees according to the first paragraph of this Article, it shall notify the employees cut down and shall, in the equal conditions, give a priority to the employees cut down." *Id.*

¹⁶³ Labor Contract Law art. 41.

¹⁶⁴ Regulations art. 119. While these additional requirements may seem burdensome, it should be noted that they are actually in line with the International Labor Organization's Termination of Employment Recommendation.

¹⁶⁵ Law, *supra* note 18.

¹⁶⁶ *Id.* But see Labor Contract Law art. 10. Article 10 of the regulation, however, may provide some guidance because it states that "if a worker is sent from his/her original Employer to work for a new Employer for a reason other than one attributable to himself/herself, his/her years of service with the

V. AN ANALYSIS OF CHINA'S LCL SHOULD ALLEVIATE FOREIGN CORPORATIONS' CONCERNS ABOUT ENFORCEMENT AND COSTS

China's LCL provides more guidance than does South Korea's LSA, which should be sufficient to prevent abuse. It is unclear whether, in the future, LCL will be enforced discriminatorily against foreign corporations, raising the costs of doing business for these firms; however, as written the LCL does not unfairly target foreign employers. And, thus far, the law has not been wrongfully used against foreign employers.

A. *China Provides Flexibility and Clear Standards for Employers, Particularly When Compared to South Korea's Labor Standards Act*

Although China's LCL shows similarities to South Korea's employment laws, LCL provides standards that are more flexible and clear. This increased flexibility and clarity should make enforcement less burdensome, uncertain, and unfair. For instance, China's law addresses the problem of unlimited fixed-term contracts by limiting employers to two renewals.¹⁶⁷ At the same time, China provides more flexibility by not limiting the term of the fixed-term contracts; in contrast, South Korean law limits fixed-term contracts to two years.¹⁶⁸

China also specifically defines part-time or temporary workers in LCL.¹⁶⁹ Part-time workers are paid on an hourly basis, cannot work more than four hours daily, and cannot work more than twenty-four hours per week.¹⁷⁰ Their hourly pay must not be lower than the minimum wage prescribed by the local government where the employer's company is located.¹⁷¹ In exchange for these restrictions, employers need not establish written employment contracts or severance pay after termination for part-time employees.¹⁷² The LCL gives employers the opportunity to make use

original employer shall be counted as part of his/her years of service with the new Employer." Using Article 10, a merger could possibly mean that the new employer must still consider a worker's years of service with the prior employer in the determination of having open term contracts. This could potentially have an impact on a company's determination on whether to merge. Article 10, however, does provide that if the previous employer has already made severance payments to the worker, the new employer does not count the worker's years of service with the prior employer when calculating severance pay after lawfully terminating or ending an employment contract. Workers therefore do not get to benefit twice from two employers unless their working period qualifies for each employer.

¹⁶⁷ Labor Contract Law art. 14.

¹⁶⁸ *Id.* See also Act on the Protection of Fixed-term and Part-time Employees, No. 8074 (2006) (S. KOR.).

¹⁶⁹ Labor Contract Law art. 68.

¹⁷⁰ *Id.* art. 68.

¹⁷¹ *Id.* art. 72.

¹⁷² *Id.* arts. 69 and 71.

of part-time workers; but, given the limited hours, it does not deter employers from using them in place of regular workers.

The implementing regulations of LCL also address protections for temporary workers. Although the law itself does not mention temporary workers, Articles 27 through 32 of the regulations provide protections for such workers. The law requires employers to inform temporary workers of the job requirements for their position, provide them with the necessary training, pay them the same amount as other workers doing the same job, and most importantly, abide by state labor standards relevant to their positions.¹⁷³ Temporary workers are also subject to severance pay.¹⁷⁴ Hence, while employers may hire workers on a temporary basis, LCL contains fewer loopholes, and better protects such workers, than does South Korea's LSA.

In contrast to South Korea's LSA, China's LCL provides clearer guidance and examples for its equivalent managerial urgency requirement. As discussed above,¹⁷⁵ the managerial urgency provision of LSA permits employers to dismiss open-term employees under certain exigent administrative circumstances, but supplies only broad categories to indicate what circumstances qualify.¹⁷⁶ By contrast, LCL supplies fourteen circumstances under which an employer may terminate a contract.¹⁷⁷ While there may be nuances to the interpretation of the fourteen circumstances, the examples limit the adjudicating tribunal's discretion and give employers a better sense of what events qualify for termination. While LCL and its regulations do limit the reasons for termination, such limits are reasonable in that they balance the competing interests of employers and their workers.

The initial reactions to LCL's impacts and enforcement have been positive. Based on statistics from twenty-six provinces, municipalities, and autonomous regions, Minister of Human Resources and Social Security Yin Weimin stated that, as of June 2008, the percentage of workers by region that had signed employment contracts is now between ninety to ninety-six percent.¹⁷⁸ While there is not yet much data on issues dealing with termination, a few months after the law's passage, a Hitachi worker was

¹⁷³ Regulations art. 29. "An employer shall fulfill its obligations set forth in Article 62 of the Employment Contract Law and safeguard the legitimate rights and interests of the dispatched employees." *Id.*

¹⁷⁴ Regulations art. 31. "Economic compensations to be made after a labor dispatch entity or a dispatched employee has lawfully dissolved or terminated the employment contract shall be made according to Articles 46 and 47 of the Employment Contract Law." *Id.*

¹⁷⁵ See *supra* Part IV.B.2.

¹⁷⁶ Kitt, *supra* note 134, at 459-553.

¹⁷⁷ Regulations art. 19.

¹⁷⁸ *Contract Law 'Boost for Social Security,' supra* note 83.

properly fired even though she had signed an open-term contract.¹⁷⁹ She was fired for disobeying orders and continually making errors in her work.¹⁸⁰ Although this is just one case, it supports the contention that Article 14 and its implementing regulations have enabled termination when justified. To further ensure consistent enforcement across jurisdictions, China could invest in training programs to better educate and equip local officials and their related institutions.¹⁸¹

While LCL regulates fixed-term contracts, it also provides clear guidelines for indefinite-term contracts so that employers have a solid understanding of termination circumstances. The guidelines will help make termination justifications uniform on a national level, reducing unequal enforcement of LCL. Additionally, by putting limits on fixed-term contracts, workers are better protected; employers can no longer use fixed-term contracts to avoid the obligations that accompany full employment. Standards for protecting temporary and part-time workers should also deter employers from substituting part-time workers for regular workers, reducing concerns of an unstable workforce like South Korea's.

B. *The LCL Has Not Been Used to Unfairly Target Foreign Employers*

The LCL has been enforced primarily against domestic, rather than foreign, employers. Most multinational corporations already comply with local labor laws and regulations in their Chinese facilities.¹⁸² Generally, the companies that complied with the Labor Law have not been as affected by enforcement of LCL.¹⁸³ It is even likely that, over the long term, LCL will actually help big, foreign corporations due to the law's impact on smaller, local competitors who did not comply with the Labor Law, and who will now be forced to adapt.¹⁸⁴ Big corporations might therefore have an advantage. In fact, foreign investment in China has continued to grow since LCL's enactment.¹⁸⁵ Some European governments also find laws like LCL

¹⁷⁹ *Employee with Non-Fixed Term Contract Fired*, CRI (July 16, 2008), available at http://www.china.org.cn/living_in_china/news/2008-07/16/content_16019118.htm.

¹⁸⁰ *Id.*

¹⁸¹ AmCham-China, *supra* note 114, at 114.

¹⁸² Winston Zhao & Owen D. Nee, Jr., *Ensuring Compliance with China's New Labor Laws*, in *DOING BUSINESS IN CHINA* 149, 159 (Practising Law Institute eds., 2008).

¹⁸³ *Id.* See also ANITA CHAN, *supra* note 3, at 261 (where the U.S. China Business Council claimed that U.S. companies tended to have standards that exceeded local law and that workplace violations in U.S. owned companies rarely had the workplace violations seen prevalent in local companies); Dan Harris & Brad Luo, *The Impact of China's Labor Contract Law*, China Law Blog (Harris & Moure), Sept. 15, 2008, http://www.chinalawblog.com/2008/09/the_impact_of_chinas_labor_con.html (last visited Feb. 1, 2009).

¹⁸⁴ Adams & Ko Shu-ling, *supra* note 120.

¹⁸⁵ Harris & Brad Luo, *supra* note 183.

helpful in conducting business in China and view them in a positive light.¹⁸⁶ Generally, profitable Western companies are not leaving China as a result of the law, despite prior threats.¹⁸⁷

Consequently, it appears that LCL has not been unequally or unfairly enforced against foreign companies and employers. Enforcement actions brought against domestic companies, like the case of Huawei Technologies discussed above,¹⁸⁸ indicate that LCL will be applied equally to both domestic and foreign employers. When Huawei, one of China's largest producers of telecommunications equipment, tried to influence workers to quit and sign new employment contracts with the intention of avoiding open-term contracts, authorities in Guangdong province's court and arbitration committee designed a new set of regulations that would have made such a maneuver illegal.¹⁸⁹

VI. CHINA'S LCL WILL HELP ACCOMMODATE CHINA'S GROWING ECONOMY

In addition to improving the general workers' condition, LCL and its regulations will help pave the way to an increasing focus on value-added industries, such as technology and services to better improve the economic progress of China.¹⁹⁰ Having a stable, dependable, and cooperative workforce is crucial to develop these industries. Open-term contracts can help China achieve that goal.¹⁹¹ Additionally, studies from other countries show that open-term contracts do not generally create widespread unemployment and may actually prove beneficial to the economy.¹⁹²

A. *China Is Shifting Its Economy to Value-Added Industries That Will Require Better Employment Relations*

In response to some negative effects from manufacturing industries, cities in China have been shifting their focus to value-added industries.¹⁹³

¹⁸⁶ *European Companies Expect More Business in China*, PEOPLE'S DAILY ONLINE, Sept. 10, 2008, available at <http://english.peopledaily.com.cn/90001/90776/90883/6497168.html>.

¹⁸⁷ Harris & Brad Luo, *supra* note 183.

¹⁸⁸ See *supra* Part IV.B.1.

¹⁸⁹ Chen Hong, *supra* note 124.

¹⁹⁰ See ALEXANDRA HARNEY, *THE CHINA PRICE* 145 (2008).

¹⁹¹ See Gosta Esping-Anderson & Marino Regini, *Introduction*, in *WHY DEREGULATE LABOUR MARKETS?* 3 (Gosta Esping-Anderson & Marino Regini eds., 2000).

¹⁹² *Id.*

¹⁹³ HARNEY, *supra* note 190, at 144.

Manufacturing provides the least amount of profits globally.¹⁹⁴ It has resulted in serious social and environmental problems in some of China's biggest cities.¹⁹⁵ For instance, Beijing encourages foreign investment in industries that bring China more expertise, technology, and better jobs instead of industries in the low-end sector.¹⁹⁶ Other cities want to make similar changes. For instance, Guangdong is moving away from its emphasis on the export-processing industry.¹⁹⁷ While the industry made Guangdong one of China's wealthiest cities, workers' rights were constantly violated while local officials turned a blind eye.¹⁹⁸ Turnover was extremely high, and corporations violated environmental and labor laws.¹⁹⁹ Value-added industries, on the other hand, not only make greater profits, but also tend to require a better-trained workforce, which requires more investment to retain and train workers.²⁰⁰ In this light, China's focus on changing its dominant industries can lead to better social relations, in addition to better profits. However, if China is to move towards having a high-value market, it will need a stable, dependable and cooperative workforce.²⁰¹ Not ensuring stability may result in a long-term lag in productivity, causing the country's industries to be less competitive globally.²⁰²

B. Open-Term Contracts Can Aid China's Industrial Shift While Protecting Workers

The LCL will create better worker protections, which, in turn, should facilitate China's move towards value-added industries and increased economic growth.

1. The LCL Restricts Fixed-Term Contracts and Encourages Open-Term Contracts, Which Will Improve Workers' Conditions and Create a Workforce Suitable for Value-Added Industries

The LCL's limits on fixed-term contracts in favor of open-term contracts will help China in its goal of improving employment relations. This improvement could, in turn, increase harmony and profits at the same

¹⁹⁴ Xiang Bing, *A New Playbook for China's Manufacturers: Making Sense of a Changing Economic Landscape*, CHINA BRIEF, May 2008, at 18.

¹⁹⁵ See HARNEY, *supra* note 190, at 93, 144.

¹⁹⁶ Adams & Ko Shu-ling, *supra* note 120.

¹⁹⁷ *Id.*

¹⁹⁸ *Id.*

¹⁹⁹ *Id.*

²⁰⁰ *Id.*

²⁰¹ Esping-Anderson & Regini, *supra* note 191, at 3.

²⁰² *Id.*

time. Other countries' experiences have shown that open-term contracts may provide more benefits than fixed-term contracts.²⁰³ Open-term contracts can help foster China's goals of social consensus and equality.²⁰⁴ Regulations expanding the use of open-term contracts can help offset the inequalities of income created by the market and increase competitive advantages.²⁰⁵ On the other hand, emphasis on fixed-term contracts can increase the poverty risk for workers, which may result in social dissension.²⁰⁶

Open-term contracts often reduce turnover while encouraging worker loyalty, which helps employer profits and long-term growth.²⁰⁷ Open-term contracts not only improve employee welfare but also efficiency, especially in industries choosing to compete on quality rather than on mere price.²⁰⁸ Open-term contracts stimulate commitment and cooperation in the employment relationship. Studies show that, as a result, both parties invest more in training, which increases productivity.²⁰⁹

Along similar lines, LCL's encouragement of open-term contracts requires interaction among employers and workers, which can prove beneficial for the employer's business. Although Article 14 will increase transaction costs for employers by requiring them to ensure that their manuals and contracts are in compliance, it will also generate clearer expectations for both parties by forcing employers to articulate the details of the work relationship.²¹⁰ According to one firm's study conducted before the enactment of LCL, Chinese workers cited dissatisfaction with their compensation and benefits and noted that they did not know how their performance was being measured.²¹¹ However, open-term contracts may affect certain groups negatively.²¹² Better protection of workers and fixed

²⁰³ See Esping-Anderson & Regini, *supra* note 191, at 3-4.

²⁰⁴ *Id.* at 1.

²⁰⁵ See Marino Regini, *The Dilemmas of Labour Market Regulation*, in *WHY DEREGULATE LABOUR MARKETS?* 12 (Gosta Esping-Anderson & Marino Regini eds., 2000).

²⁰⁶ Catalina Amuedo-Dorantes & Ricardo Serrano-Padial, *Fixed-Term Employment and Its Poverty Implications: Evidence from Spain*, *FOCUS* Vol. 23, No. 3 (Spring 2005), at 42. Please note that the study on determining different reactions to employment contracts was conducted in Spain only.

²⁰⁷ Luis Toharia, *Comments*, in *SOCIAL DIMENSIONS OF EMPLOYMENT* 47 (Antonio Argandoña & Jordi Gual eds., 2002); Regini, *supra* note 205, at 24.

²⁰⁸ See Esping-Anderson & Regini, *supra* note 191, at 3.

²⁰⁹ See Gosta Esping-Anderson, *Who Is Harmed by Labour Market Regulations? Quantitative Evidence*, in *WHY DEREGULATE LABOUR MARKETS?* 71 (Gosta Esping-Anderson & Marino Regini eds., 2000).

²¹⁰ See US-China Business Council Staff, *supra* note 112, at 49.

²¹¹ Ed Emerman & Emily Rieger, *Dissatisfaction With Pay, Benefits Widespread in China*, *Watson Wyatt Finds*, Mar. 2007, available at <http://www.watsonwyatt.com/news/press.asp?ID=17167>.

²¹² Gosta Esping-Anderson & Marino Regini, *Conclusions*, in *WHY DEREGULATE LABOUR MARKETS?* 337 (Gosta Esping-Anderson & Marino Regini eds., 2000).

labor costs from open-term contracts has been shown to increase unemployment, particularly among the low-skilled work force.²¹³ This could be problematic in China, given that there is a huge population of low-skill workers. One should keep in mind that fixed-term contracts are still permitted under LCL and that options still exist to blunt potential negative effects of open-term contracts. Fixed-term contracts will continue to be used by employers where their use gives workers better incentive to be productive.²¹⁴

The limitations LCL places on the use of fixed-term contracts are appropriate given the negative impacts that pervasive use of short fixed-term contracts have on the workforce. There is no evidence that providing fixed-term contracts boosts long-term economic growth or creates higher levels of employment.²¹⁵ Studies show that low employment security results in workers' lack of identification with and loyalty to the corporation. That lack of worker investment leads to under-investment in human resource development, with workers not being encouraged to pursue further training.²¹⁶ For example, studies show that fixed-term contracts, as compared to open-term contracts, in the United States and Spain have led to decreased job stability, lower pay, worse working conditions, frequent periods of unemployment, and higher poverty risk.²¹⁷ In Spain, fixed-term contracts have not created incentives for employers to rehire workers.²¹⁸ South Korea, as mentioned earlier, is a prime example of some negative effects of short fixed-term contracts.²¹⁹ Hence, having only fixed-term contracts can hinder national competitiveness and may actually exacerbate unemployment in certain circumstances.²²⁰

China's LCL balances the interests of employers and workers by making open-term contracts the default mode for long-term employment, but also allowing limited use of fixed-term contracts. While LCL clearly affords some preference to open-term contracts, permitting fixed-term contracts will help preserve employment opportunities for the low-skill workforce. Additionally, LCL's preference for open-term contracts will help transition China's economy to more value-added industries.

²¹³ *Id.*

²¹⁴ See Theodore Groves et al., *Autonomy and Incentives in Chinese State Enterprises*, THE Q. J. OF ECON. 183, 208 (Feb. 1994).

²¹⁵ See Esping-Anderson, *supra* note 209, at 72.

²¹⁶ See Kitt, *supra* note 134, at 561; JONES, *supra* note 137, at 43.

²¹⁷ See Amuedo-Dorantes & Serrano-Padial, *supra* note 206, at 42.

²¹⁸ See Esping-Anderson & Regini, *supra* note 212, at 340.

²¹⁹ See *supra* Part IV.C.

²²⁰ See Regini, *supra* note 205, at 26.

VII. CONCLUSION

China's transition from a planned economy to a market economy has resulted in growing inequality and worker exploitation. China enacted the Labor Law in 1994, but its requirement that employers use employment contracts was weakly enforced, due in part to unclear expectations among both employers and workers. The deficiencies of the Labor Law left many workers unprotected and insecure, which began to threaten the stability of China's workforce.

The enactment of LCL in 2008 came at a crucial time. It addressed many of the gaps left by the Labor Law. With LCL's expanded and explicit support of open-term contracts, both workers and employers better understand the law governing employment relationships. The LCL prompts employers to be more explicit in their requirements, creating clearer expectations for both employers and workers, which should in turn lead to better relations. The LCL also increases protection for workers without preventing employers from terminating employees for just cause. While Article 14 does not completely resolve the issue of whether an employer is obligated to renew a second fixed-term contract,²²¹ foreign companies should not feel threatened by the possibilities of having open-term contracts. Open-term contracts will not constitute employment for life, nor will their protections under LCL prove as inflexible as similar provisions in South Korean labor law.

Open-term contracts may also aid China in its transition into a more high-value, industrialized economy. While LCL does not target foreign companies, it remains unclear whether the law will be enforced appropriately—particularly because the regulations were passed very recently. Foreign corporations will likely need more time to evaluate the law's impact on their daily business. Yet, they can be assured that LCL does not amount to a reversion to the "iron rice bowl" system. It is now up to the Chinese government and local tribunals to realize LCL's promise.

²²¹ See *supra* Part IV.C.2.